

**2006 ANNUAL REPORT
OFFICE OF STATE LANDS & INVESTMENTS**

Wyoming Quality of Life Result

Wyoming natural resources are managed to maximize the economic, environmental and social prosperity of current and future generations.

Agency

Office of State Lands & Investments

Contribution to Wyoming Quality of Life

Wyoming School trust assets are managed, preserved and enhanced through responsible stewardship to contribute directly to the economic, social and environmental well being of Wyoming's public school children, local communities and natural resources.

Basic Facts

Statutory Authority: Organic Act, Sec. 14; Act of Admission, Sec. 4 through 14; Wyo. Const. Art. 7, Sec. 2, Sec. 6 through 8, Sec. 18, 19 and 22; Wyo. Const. Art. 18, Sec. 1, 2, 3, 4, 5, 6; W.S. 7-16-202; W.S. 8-4-102; W.S. 9-4-305, W.S. 9-4-307 through 111; W.S. 9-4-601 through 607; W.S. 9-4-701, 703, 704 and 708 through 713; W.S. 9-4-801 through 815; W.S. 9-4-1001 through 1002; W.S. 11-31-131; W.S. 11-34-101 through 305; W.S. 16-1-109 and 110; W.S. 16-1-201 through 207; W.S. 16-1-301 through 308; W.S. 21-15-106 and 111; W.S. 27-14-701 through 704; W.S. 36-1-101 through 36-3-111; W.S. 36-5-101 through 36-7-510; W.S. 36-9-101 through 120; W.S. 36-12-102, 106 and 107; W.S. 41-6-203 through 209.

Organizational Structure: The Office of State Lands & Investments consists of the Office of the Director and five divisions: Financial Programs and Management Services, Real Estate Management and Farm Loans, Mineral Leasing and Royalty Compliance, Information Technology, and Wyoming State Forestry. The Real Estate Division has one field office located in Lander. The Wyoming State Forestry Division has seven district offices located in Newcastle, Buffalo, Riverton, Lyman, Pinedale, Casper and Douglas.

Staff & Budget: The agency is supported by 98 full time employees (48 Forestry Division, 50 remaining divisions) and four seasonal Forestry Division employees. The FY06 agency budget was \$62,746,931: \$23,542,262 general funds, \$17,833,983 federal funds and \$21,370,686 other funds.

People served: Collectively, these divisions serve the trust beneficiaries - Wyoming's school children and state institutions; numerous clients in agriculture, mineral, timber, transportation, communication, public utility, recreation, tourism and other Wyoming industries; local government entities; state and federal agencies; and the resident and non-resident general public.

Five most important functions:

Optimization and diversification of trust asset revenue:

- design and perform effective mineral royalty, mineral lease and agricultural lease compliance, collection and fund distribution functions;
- develop a proactive commercial leasing program; and
- optimize benefits gained through easements, forest product sales and trust land sales.

Preservation and enhancement of trust asset values for current and future beneficiaries:

- employ efficient, effective and proactive land management practices, including the pursuit of land sale, acquisition and exchange opportunities that will generate access to contiguous land parcels to facilitate efficient trust land management practices;
- control and eradicate noxious weeds and designated pests;
- use lease stipulations to protect surface and subsurface resources; and
- conduct efficient and effective inspection, bonding and reclamation programs.

Forestry assistance:

- provide technical assistance, training, and support to local governments, cooperating agencies, and citizens through optimum utilization of state funding to leverage federal and local funds to attain sustainable management and protection of the state's natural resources.

Grant and loan program administration:

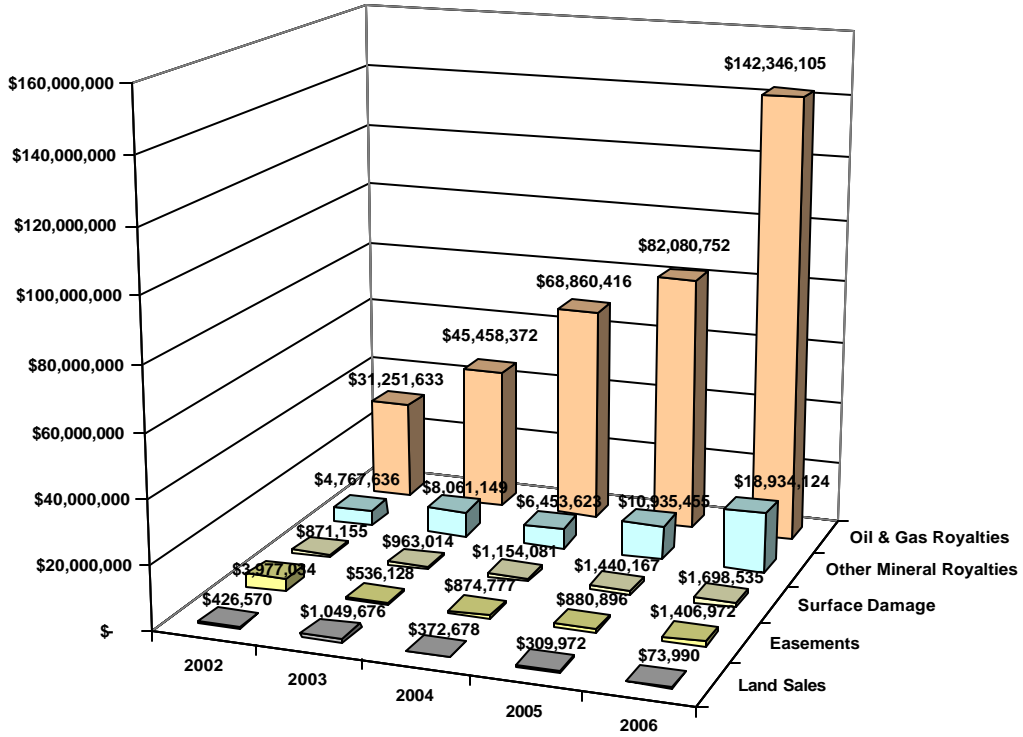
- assist the State Loan and Investment Board in optimum utilization of program funding through timely and accurate project eligibility evaluations and analysis to address the specific needs of local communities;
- explore and utilize opportunities to partner with similar state and/or federal programs to maximize funding availability to benefit local communities.

Data development and data sharing:

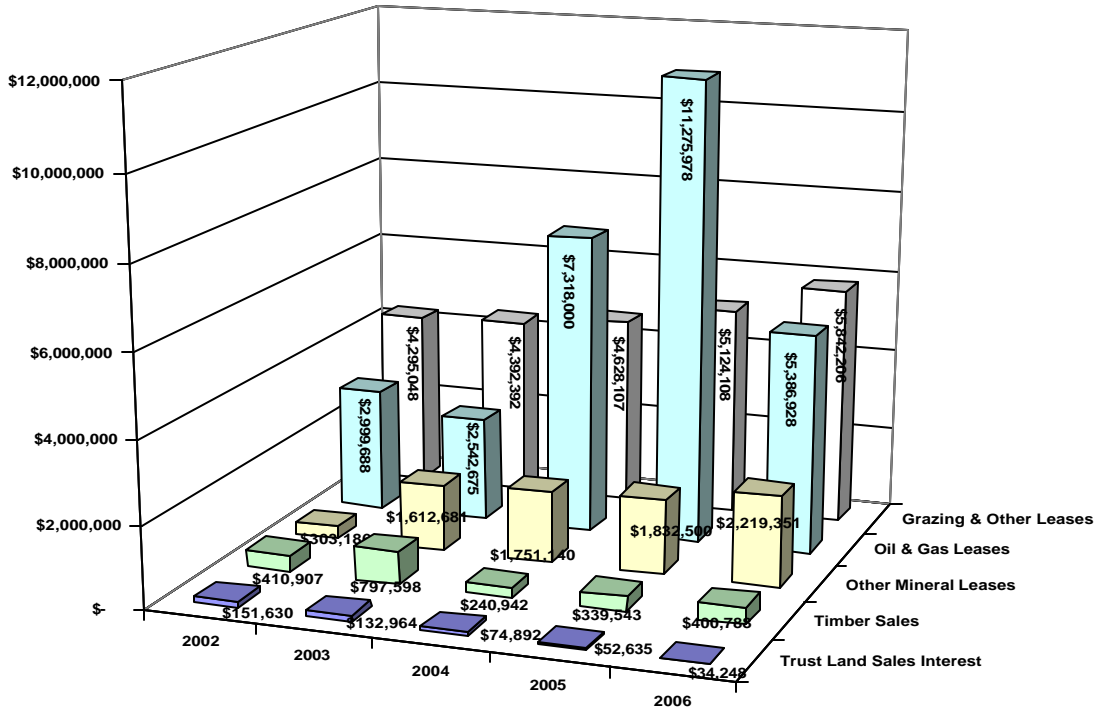
- utilize technology and improve systems to monitor all classes of trust assets and administer leases of all types to improve reporting capability for the evaluation of the physical condition, maintenance and productivity of trust assets;
- coordinate, encourage uniformity, promote data sharing and gain efficiency in the agency's architecture and standards to ensure compatibility of information technology related projects with other state, federal and local agencies.

PERFORMANCE MEASURE #1
Optimization and Diversification of Trust Asset Revenue

Graph 1. Trust Asset Revenue and Impact Payments Distributed to Permanent Funds



Graph 2. Trust Asset Revenue Distributed to Income Funds



**Story Behind the Last Year of Performance – Performance Measure #1:
Optimization and Diversification of Trust Asset Revenue - Graphs 1 and 2.**

Although revenues fluctuate from year to year, mineral leasing and development provide the greatest revenues from state trust lands. Royalties are directly affected by market place economics; higher commodity prices increase royalties collected for oil, gas and other minerals as reflected in Graph 1. In FY06 oil, gas and other mineral royalties generated 98.06% of the total trust asset revenue distributed to the permanent funds. Fiscal year 2002 brought increased prices for oil, natural gas and coal. While production of oil on state lands declined in this period, natural gas and coal production increased. Prices for all commodities rose in FY03 and production held through the year. Fiscal year 2004 prices for natural gas and oil increased approximately 31% over the prior years. Fiscal year 2005 oil prices increased while gas prices held at 2004 levels; and production remained stable. In FY06 mineral royalty revenue distributions increased 73.38% above those in FY05.

Inasmuch as this agency strives to have as much viable acreage under lease at any one time for minerals, the leasing of state land for mineral production and return on that activity is significantly dependent on product price and the viability of the area available for lease. At the close of FY06 the trust had 5,452 active oil, gas and other mineral leases encompassing 2,312,460 acres, of which 1,304 leases and 520,534 acres were held by production. The trust realized a 3.29% increase in the total number of acres under lease from FY05 to FY06 and an increase of 6.87% in the number of acres held by production during that period.

The number of surface acres under lease remains relatively constant from year to year. At the close of FY06 the trust had 3,539,632 acres of surface under lease for grazing and agricultural purposes. Historically, grazing is the largest land use, and as illustrated in Graph 2, provides a consistent level of revenue from year to year. In FY06 revenues collected for all surface-related activities, excluding real estate sales and timber sales amounted to 5.01% of the total trust revenue collected during that period. Easement revenue in FY02 was significantly influenced by the final installment for a single easement, Express Pipeline, which provided an influx of \$3 million that year. Absent this major contribution, the steady upward trend for easement activities is indicative of an increase in easements for pipelines, powerlines and roadways, primarily a result of increased coal bed natural gas development activities. In addition to increased easement revenue, coal bed natural gas activities are also responsible for the continued increase in surface impact payments received by the trust for impacts caused by the development activities.

Revenue from the sale of state lands is reported on the installment sales method in the year the cash payment is received, (i.e. the principal portion of the cash received from annual contract payments). The majority of the outstanding land sale contracts relate to the sale of trust lands which occurred prior to 1996. Contract dates range from 1976 to 2006, with thirty year amortization schedules and interest rates that range from 5.5%

in 1976 to 8% at the current date. During FY 2003, interest rates offered by traditional lenders declined significantly, leveling to 5.5% at year end, while interest rates offered for state programs remained at traditional rates of 8% to 9%. The decrease in mortgage rates offered by traditional lenders afforded state borrowers the ability to refinance outstanding installment contracts at a much lower rate. As illustrated in Graph 1, the fluctuation in revenue recorded from the sale of state lands during fiscal years 2003 and 2004 is the consequence of refinancing activities. FY05 land sales revenue totaled \$309,972 which included three cash trust land sales and two contract payoffs. The FY06 land sales revenue of \$73,990 represents annual installment principal payments, one installment contract payoff, and the sale of a small home site tract for a total purchase price of \$3,500. Within any fiscal period, the land sale revenue may include cash sales and/or installment contract payoffs; therefore, the land sale interest revenue depicted in Graph 2 fluctuates.

Revenue generated from the sale of forest products is influenced by a number of factors, the greatest being the forest product market. Fiscal year 2003 recorded the highest volume with \$797,598. The majority of this revenue, \$500,000, was derived from a single contract with Louisiana Pacific. The contract was initiated in 1998 but the timber harvest was not completed until FY03. The timber market was strong in 2004 and 2005, but dropped in 2006. Despite this fact, the revenue from timber sales illustrated in Graph 2 increased in FY05 and FY06. Timber offered and sold in one fiscal year may not be paid for and/or harvested until the next fiscal year or even several fiscal years later. The price for timber is established in the original timber sale contract through competitive bid and subject to market conditions at that time. Therefore, the reverse could also be true, and revenue in any given fiscal year could appear to be lower than expected based on the timber market at the time the sales contract is executed. Timber sales continue to be affected by the increasing drought conditions and related fire activities, as well as the loss of the largest timber purchaser in the state, which reduced competition for timber sales in part of the state.

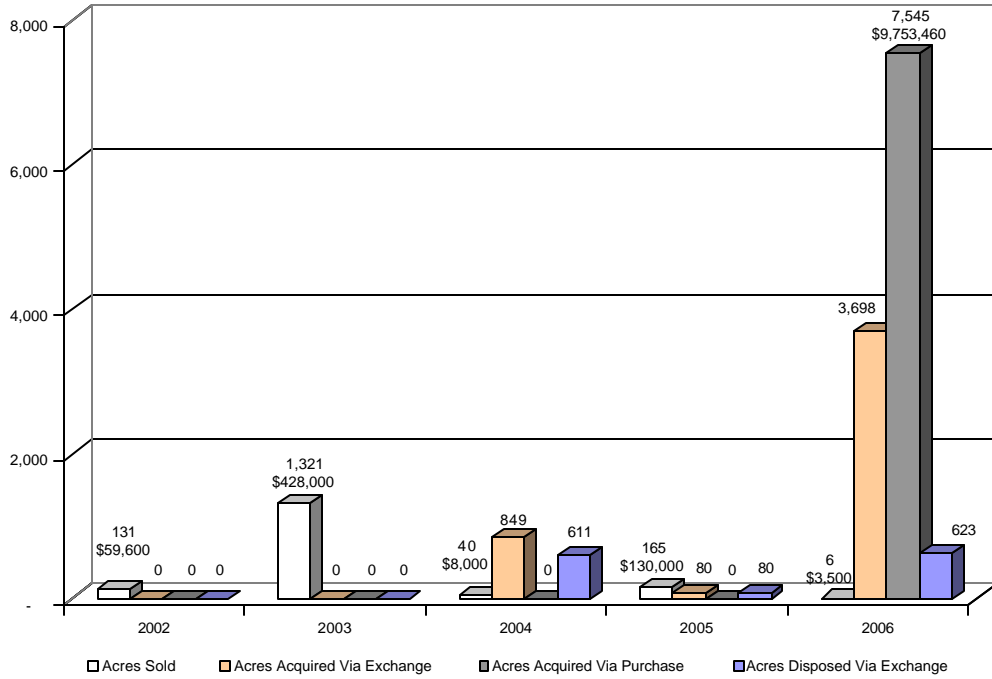
FY06 Accomplishments:

- 1) Utilizing existing Electronic Mineral Accounting Section personnel, created an Information Technology Division to facilitate and establish the internal structure necessary to improve and increase intra- and interagency efficiency and effectiveness.
- 2) Received funding in the 2006 Budget Session that will allow the Real Estate Division to accomplish the conversion of existing hard-copy data to electronic data within this biennium.
- 3) Received funding and authorization in the 2006 Budget Session for one position in the Royalty Compliance Section to assist and augment program delivery for current and foreseeable increases in royalty accounting, and the timely and accurate collection and distribution of funds to appropriate permanent and income funds.

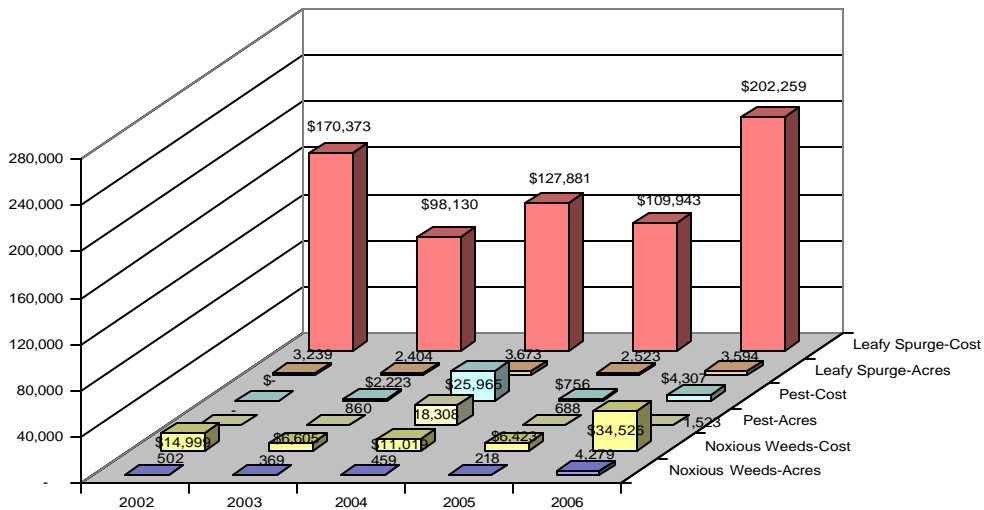
- 4) Recruited a commercial property manager that will allow the agency to employ a proactive management approach to special use leasing, including industrial, commercial, recreational and other similar use leases.

PERFORMANCE MEASURE #2
Preservation, Enhancement and Appreciation of Trust Asset Values

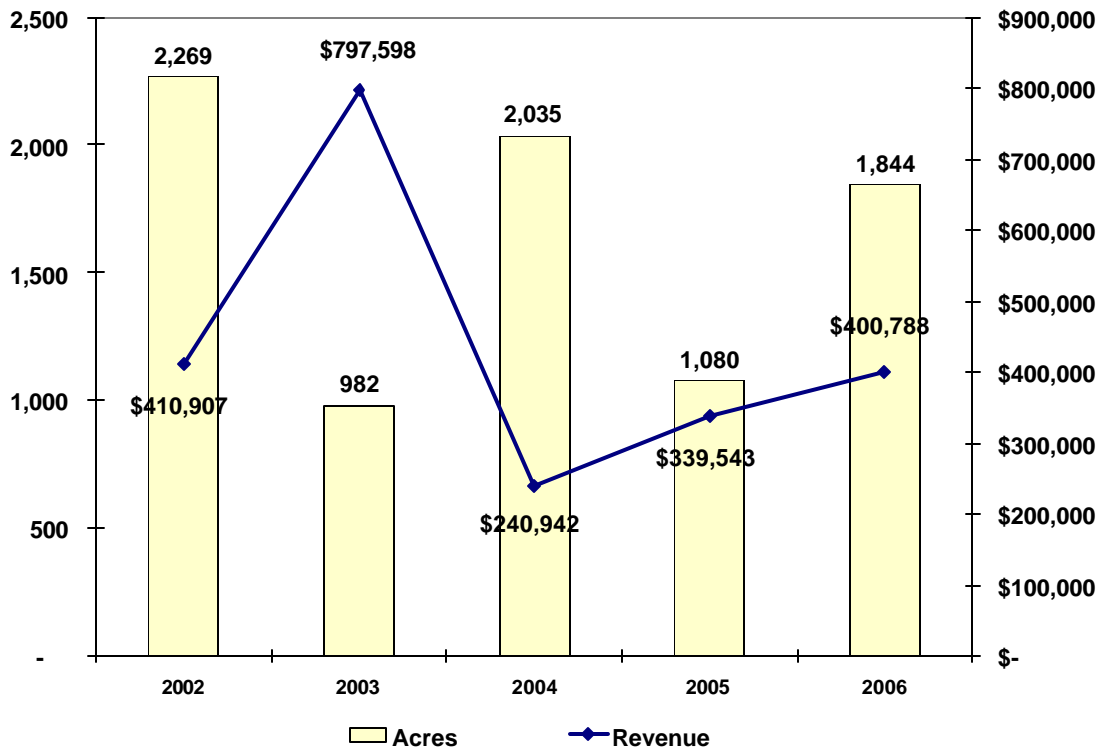
Graph 3. Trust Land Sales, Land Acquisitions, Land Exchanges



Graph 4. Noxious Weed and Designated Pest Treatments



Graph 5. Silvicultural Treatment



Story Behind the Last Year of Performance – Performance Measure #2: Preservation, Enhancement and Appreciation of Trust Asset Values - Graphs 3, 4 and 5

There has been nominal change in total amount of land in the trust’s land portfolio until FY06. In FY06, two exchanges were completed. One exchange involved a uranium mill tailings site where the State traded 640 acres of minerals within the tailings area for 320 surface acres and 640 mineral acres outside of the contaminated area. In the other exchange, the State traded 622.74 acres of state land with very difficult public access and acquired 3,378.20 acres of private land with good public access adjacent to other state and BLM land. In FY05, three sales of state land were conducted involving isolated, difficult to manage tracts. These sales resulted in 164.78 acres of state land being sold for \$130,000.00. In FY06, one 6.00 acre tract that had a residence located on it was sold for \$3,500.00.

Pursuant to W.S. 9-4-701(r) and 2006 Wyoming Session Laws, Chapter 35, the Real Estate Division completed two land purchases in FY06. The Duncan Ranch in Converse County containing 6,439.11 acres was purchased for \$5,940,000. In Sheridan County and Johnson County 1,105.56± acres of the land with historical importance surrounding Fort Phil Kearny and the Fetterman Battlefield plus the Lake DeSmet Monument fishing access was purchased for \$3,813,460. Chapter 35 further provides that there shall be no net gain of lands held for the common school permanent land fund in excess of 10,000

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acres. Between the period of July 1, 1999 and June 30, 2006, land sales, exchanges and acquisitions resulted in a net gain of 10,241.99 acres in the Common School Permanent Land Fund. Several land sales will be completed in FY07 which will reduce the net gain in the Common School Permanent Land Fund below the 10,000 acre limit.

Noxious weed and control of designated pests on state-owned land is a cooperative effort between the Office of State Lands and Investments, the grazing lessee, and County Weed and Pest Districts. Graph 4 illustrates noxious weed treatments being somewhat consistent over the years until FY06. In FY06 state lessees in twenty-one counties participated in the treatment and eradication of noxious weeds and pests as opposed to only eleven counties participating in 2002 through 2005.

Forested lands are managed to protect their long term value to the trust through the use of forest management projects or silvicultural treatments (timber sales, thinning, salvage, firewood sales, and Christmas tree sales) designed to improve forest health and productivity. Above normal fire seasons reduced the amount of time staff could dedicate to the preparation of forest management projects which impacts acres of silvicultural treatment, volume harvested, and forest products income as demonstrated in Graph 5. Although fire suppression is a top priority, lost time during the summer field season reduced the amount of time staff spent on preparation for forest management projects. Because there can be a two year lag between the offer of a forest product sale and harvest of the sale, the effects of the reduction in sale preparation time can be long lasting and may take several years of increased sale preparation effort to get the number of acres treated back to desired levels.

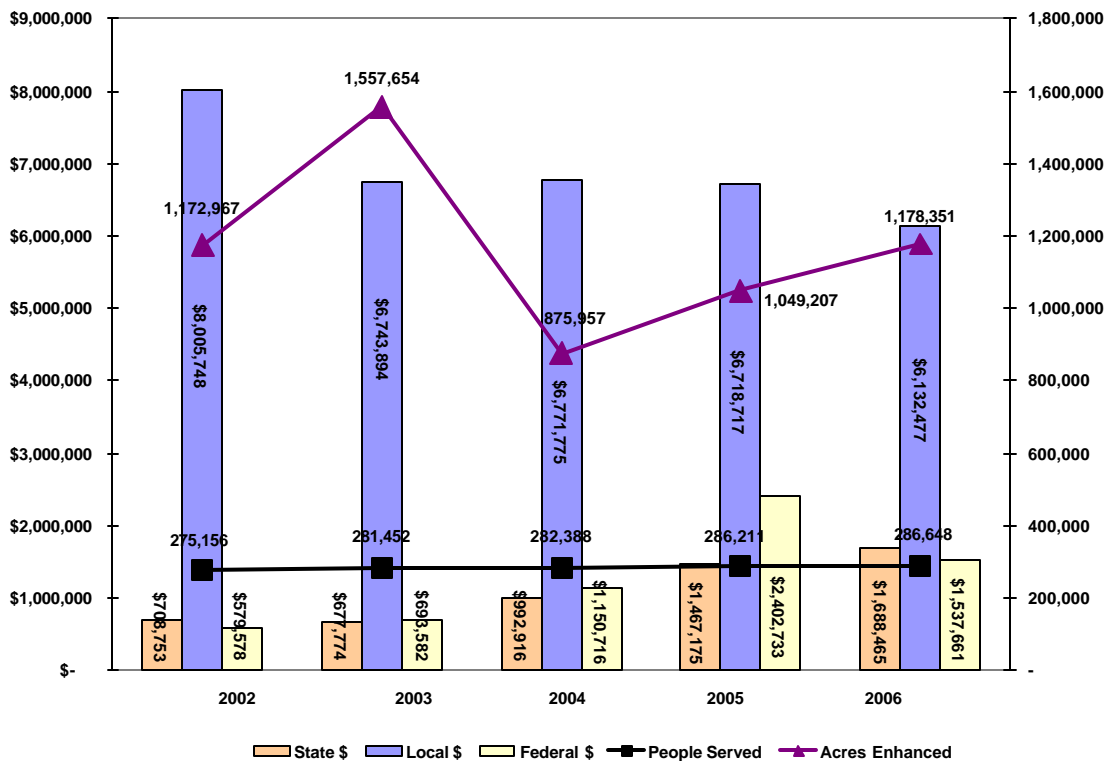
FY06 Accomplishments:

- 1) During the 2005 General Session, the Wyoming Legislature passed SF0015 that created a “trust land preservation and enhancement account” and funded the account with \$750,000 from the School Foundation Program Account. The intent of the Legislature was clear that “funds in the State Land Preservation and Enhancement Account shall be used by the Office of State Lands and Investments to fund projects which will preserve and enhance the asset value of all surface and mineral lands held in trust by the State.” A report relative to the progress and status of this account is reported to the Legislature on or before October 1 each year. In FY05 fourteen projects totaling \$105,297.50 were approved by the Board. These projects were completed in the summer and fall of 2005. In FY06, ten projects totaling \$99,990 were approved to be completed in the summer and fall of 2006.
- 2) On August 10, 2005 the Board of Land Commissioners adopted trust land management objectives that set forth controlling, prioritized criteria that is now used to evaluate all state trust land exchange, sale, acquisition and long-term lease proposals.
- 3) Received funding and authorization in the 2006 Budget Session for one position that will amplify our ability to inspect leases, weed and pest control

- activities, easements and CBM water storage reservoirs as well as investigate unauthorized and illegal activities occurring on state land surface.
- 4) Received funding in the 2006 Budget Session to contract for specialized services for the appraisal of commercial, industrial and transitional properties that current Real Estate Division staff cannot provide.
 - 5) Relocated Weed and Pest Program administration and records from the Lander field office to the main office in Cheyenne in June, 2006.
 - 6) Received funding in the 2006 Budget Session that will allow the Real Estate Division to treat noxious weed infestations and designated pests on up to 50,000 acres of state surface per year.
 - 7) Received funding in the 2006 Budget Session to provide for the necessary increase in supervisory personnel, equipment and overhead costs required for the Wyoming Honor Conservation Camp.
 - 8) The Wyoming Legislature amended W. S. 36-2-107 in the 2006 Budget Session to identify unlawful uses of state lands and provide misdemeanor penalties and peace officer enforcement related to those unlawful uses.
 - 9) Received funding in the 2006 Budget Session for repair, maintenance and enhancement projects on 9,000 acres of no n-trust institutional and acquired properties managed by OSLI.

PERFORMANCE MEASURE #3
Forestry Assistance

Graph 6. Program Utilization and Funding Assistance



**Story Behind the Last Year of Performance – Performance Measure #3:
Forestry Assistance - Graph 6.**

Assistance Forestry programs utilize state general fund dollars to leverage federal and local dollars to provide technical assistance to private landowners, communities, counties, Conservation Districts, County Volunteer Fire Departments, businesses, and numerous cooperating agencies. These programs include Urban and Community Forestry, Private Forestland Management, Fire Management, National Fire Plan, Living Snow Fence, Forest Health and the Forestry Conservation Camp program.

Graph 6 illustrates that Assistance Forestry programs serve approximately one-half of the state's population and utilizes state general fund dollars to leverage federal and local funds to provide the assistance described above. State general fund dollars are generally used for operational support as are a percentage of federal assistance dollars. The graph depicts a variation in the amount of federal grant dollars expended over the period. This can be attributed to an improvement in the utilization of grant funds through the incorporation of coordinators for individual projects primarily within the National Fire Plan project areas.

During 2005 and 2006, an increase is shown in federal grant dollars when compared with previous years. In reality, an overall decrease occurred, the bulk of which occurred within the National Fire Plan and Urban and Community Forestry programs. This disparity is due to the fact that 2002 – 2004 program numbers only reflect those federal, state and local dollars that were actually expended during the period, not the entire grant dollars awarded. Most federal grants are open for a minimum of 2 years. As previous year grants are completed and dollars expended, the federal grant amount increases. The efficiency with which federal grants have been utilized has increased as Division personnel and landowners have become acquainted with these programs, the National Fire Plan in particular.

The local dollars depicted is inclusive of all programs. The fire program is typically the dominant program and accounts for more than 50 percent of the total shown. Active fire seasons will result in significant increases in local dollars expended. The local dollars portrayed for 2006 is an estimate. Qualifying dollars are collected from October 1 through March 31 and from April 1 through September 30 of each year. Therefore, actual expenses for April 1 through September 30 are not available at this time.

FY06 Accomplishments:

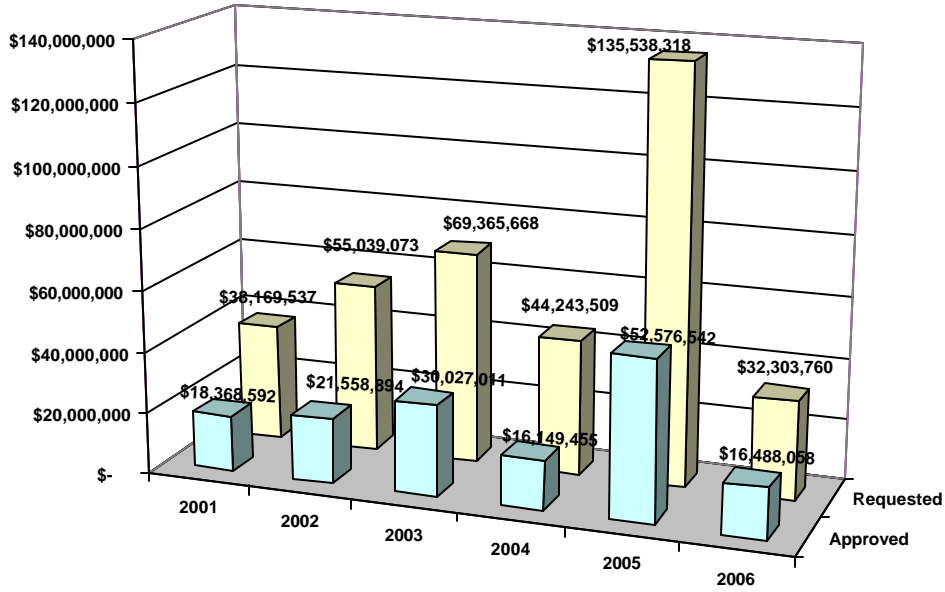
- 1) A statewide management conference for community tree board members was held in addition to several other technical workshops and presentations. The decline in federal funds is limiting the number of grants to communities for educational efforts.
- 2) The Division's list of available resource consultants was updated regionally during this period via personal contact. This list is available to the public via the Division's website and/or direct mail.

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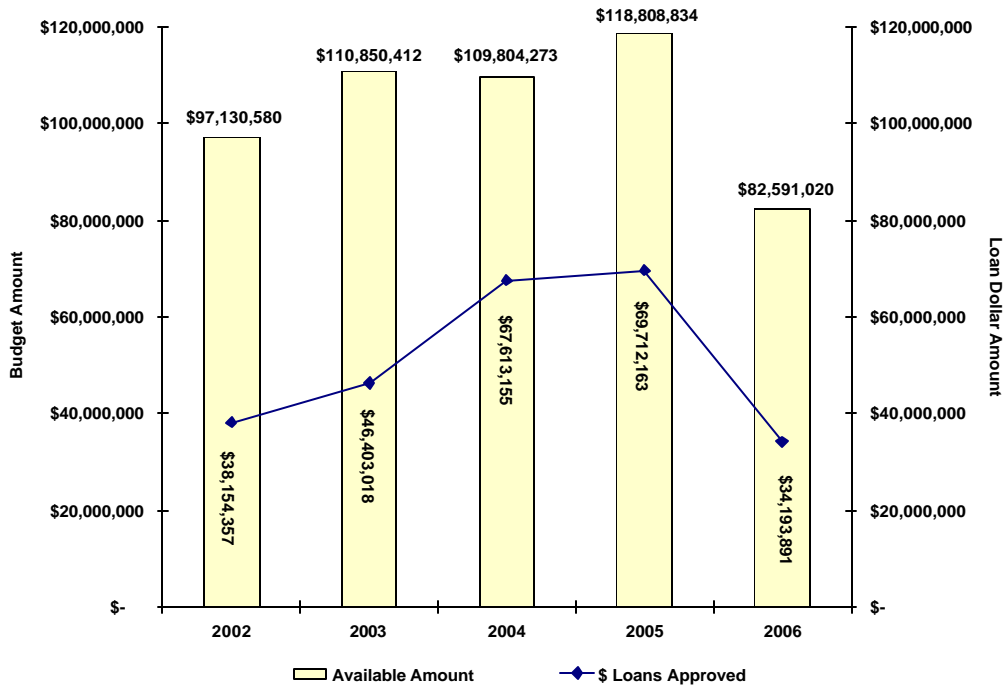
- 3) The Division hosted a “Facilitative Instructor Class” to instruct individuals on training techniques and protocol. The class was held in January 2006 with approximately 25 participating. County Volunteer Fire Departments continue to be supportive of this effort.
- 4) The Division applied for and received a grant under section (319) of the Clean Water Act to continue audits of harvest sites and update the Forestry BMP Field Guide. This Guide is consistent with the silvicultural BMPs adopted by the Wyoming Department of Environmental Quality.
- 5) More than 50 percent of National Fire Plan (NFP) projects within the state are now under the direction of a local project coordinator. This has increased the efficiency of project implementation and effectiveness of projects. Competition for NFP dollars will limit program dollars received. Numerous fire and resource related agencies are cooperating and supportive of the NFP project in the state.
- 6) A statewide workshop was held to educate Conservation District employees on the design and maintenance of agroforestry related applications. This was done with the cooperation and support of the Natural Resources Conservation Service (NRCS) and WY Association of Conservation Districts. Work continues on a daily basis to provide technical assistance as requested. Reduced federal funding is and will continue to impact availability of technical resources in the area.
- 7) The Division worked cooperatively with the USGS to digitize and assign attributes to forested land within the state. Private forested lands in the state are being spatially analyzed through a 13 layer analysis to facilitate better use of Division resources.
- 8) In 2006, 29 agencies were assisted through the Conservation Camp program. Wild fire fighting assignments, considered the highest priority of work projects, continue to limit assistance to other agencies outside of fire suppression.

Performance Measure #4
Grant and Loan Administration

Graph 7. Grant Program Utilization and Funding Assistance



Graph 8. Loan Program Utilization and Funding Assistance



**Story Behind the Last Year of Performance – Performance Measure #4:
Grant and Loan Program Administration – Graphs 7 & 8**

A portion of grant program funding is designated by statute, appropriated through legislative authority and is set at \$37 million per biennium. That portion of the Mineral Grant Program (MRG) funding, \$35 million, is provided from Federal Mineral Royalty distributions. Transportation Enterprise Program (TEA) funding, \$2 million per biennium, is provided from interest earnings from the Transportation Trust Fund and is limited to 90% of the interest earned on the cash balance of the trust fund.

Funding for the 2005/2006 biennium increased to \$67.4 million with additional appropriations from the general fund in the amount of \$28 million and \$4.4 million. Grants from the biennial appropriation are distributed at the discretion of the State Loan and Investment Board at several grant and loan meetings over the course of the biennium. During FY2005 the Board allocated a greater portion of the appropriated dollars, \$52.6 million, for projects requests; leaving less available funding, \$16.5 million dollars, for awards in FY2006. As illustrated in Graph 7, while available program dollars show an increase during the fiscal years presented, the needs of the local communities increased at a greater rate. Requests for project funding continued to escalate in fiscal years 2005 and 2006 exceeding available program funding by \$98.8 million.

The loan programs depicted in Graph 8 include the Clean Water State Revolving Fund Program (CWSRF), the Drinking Water State Revolving Fund Program (DWSRF) and the Joint Powers Act Loan Program (JPA). Requests for dollars increased significantly during fiscal years 2005 and 2006 bringing the average available dollars to \$91.1 million, \$62.6 million in cumulative federal program dollars and \$28.5 in state program dollars.

The use of project funding offered through the JPA program has shown a decrease in demand in recent years. Program funding is provided by statute from the state's Permanent Mineral Trust Fund and is set at \$30 million dollars. Available funding for the JPA program during any fiscal year is the net of the total program funding, \$30 million, less the outstanding loans for the period. A decrease in market interest rates offered by traditional lenders, as well as the use of bonding authority for capital construction projects, contributed to the decline in new and outstanding loans during fiscal years 2005 and 2006.

FY06 Accomplishments:

- 1) Received funding and authorization in the 2006 Budget Session for one State Revolving Fund Program position. This new position will enable the program to provide efficiencies in loan processing and services to local communities in meeting project funding requests.
- 2) Grant and loan programs under the management of OSLI partnered with state and federal programs to provide full project funding in the amount of \$52.1 million to local communities during FY05 and FY06. Agency program funding totaled \$45 million, with other state funding of \$6.8 million and local funding of \$300,000.

- 3) During the 2005 General Session of the Legislature, the agency assisted the Board in securing additional legislative funding in the amount of \$28 million for Mineral Royalty Grant Program to fund local community project requests, \$10 million of which was specifically designated for grants to local governments impacted by natural resource development.

Supplemental Budget Implications

Priority #1: Recommendations of the Legislative-Executive Task Force - IT (Information Technology) resources to automate business processes and staffing for key trust management functions.

The Wyoming State Legislature created a 15-member, joint executive-legislative task force in 2005 to “**review funding for the Office of State Lands and Investments’ trust programs.**” The Report and Preliminary Recommendations the Task Force submitted to the Wyoming State Legislature on June 1, 2006, the State Lands Task Force recommended additional investment in three critical administrative areas of the Office of State Lands and Investments: (a) IT resources to automate business processes and manage and report trust asset data; (b) additional staffing for key trust management functions related to royalty payment compliance and real estate planning and valuation; and, (c) additional monies for capital investment and professional services that will increase rental/royalty returns, increase the underlying value of the land and mineral assets in the trust portfolio, and/or reduce asset management costs. These recommendations, if implemented, will commence an incremental, performance-based course toward more efficient and effective trust asset management.

Pursuant to the State Lands Task Force Recommendations, the supplemental budget request is intended to timely address important and immediate information and technology needs and staffing shortages that impact the Board’s and Office’s ability to effectively manage the State’s trust assets in a rapidly changing land and mineral business environment.

A total of \$895,543 is requested for funding two of the identified critical areas:

- (a) IT resources to automate business processes and manage and report trust asset data; and,
- (b) additional staffing for key trust management functions related to royalty payment compliance and real estate planning and valuation.

Details of these requests are found in Surface/Real Estate Management and Farm Loan Division, Eorg 0102, Section 2, Supplemental Budget Request, Subsurface/Mineral Leasing and Royalty Compliance Division, Eorg 0107, Section 2, Supplemental Budget Request and Information Technology Division, Eorg 0109, Section 2, Supplemental Budget Request. Requested funding for this request is 100% General Fund.